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FEDERAL COMMUNICATIONS COMMISSION
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BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

In the Matter of	)	
	)	
Local Exchange Carriers' Rates, Terms, and Conditions for Expanded Interconnection Through Virtual Collocation for Special Access and Switched Transport	)	CC Docket No. 94-97, Phase I
	)	DOCKET FILE COPY ORIGINAL

REBUTTAL OF SOUTHWESTERN BELL TELEPHONE COMPANY

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April 11, 1995

CC Docket No. 94-97
Phase I

Rebuttal Of
Southwestern Bell Telephone Company

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SUMMARY*

The Oppositions to SWBT's Direct Case have engaged in a classic case of "picking and choosing" which arguments of SWBT to which they wish to respond, and ignoring those arguments to which they cannot respond. Thus, the major flaws in the positions of the Oppositions are highlighted.

For example, only a few Oppositions attempted to address SWBT's comparison of virtual collocation rates to DS3 rates, and none were able to prove that the comparison did not show that SWBT's virtual collocation rates are overly discounted. Also, SWBT's citation to the CC Docket No. 83-1165 proceedings, which defined "service" as something other than what it is being used for in this docket, stands unchallenged, other than by a few summary arguments which do nothing to disprove the correctness of SWBT's position.

SWBT's Rebuttal also details, again, the reasons for keeping SWBT's cost support, including the data in its Direct Case, confidential. None of the Oppositions provides any good argument to release SWBT's proprietary cost data, and some of the Oppositions fail to even acknowledge that the Bureau has already determined that the cost data is confidential.

SWBT's Rebuttal further defends SWBT's recovery of overhead through its NRCs in its virtual collocation rate structure. No Opposition has provided any basis to show that

* All abbreviations used herein are referenced within the text.

SWBT's rate structure is unreasonable due to this method, or for any other reason.

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REBUTTAL OF
SOUTHWESTERN BELL TELEPHONE COMPANY

Southwestern Bell Telephone Company (SWBT), pursuant to the Designation Order released February 28, 1995 by the Common Carrier Bureau (Bureau),[1] hereby files its Rebuttal in this matter.[2]

I. SWBT'S FILINGS ARE PROPERLY TREATED AS CONFIDENTIAL.

A number of the oppositions claim that SWBT has wrongly attempted to protect its confidential cost and overhead data.[3] However, none of these Oppositions can justify their desire to view the data. Without a sufficient reason to view SWBT's confidential

[1] Local Exchange Carriers' Rates, Terms and Conditions for Expanded Interconnection Through Virtual Collocation for Special Access and Switched Transport, CC Docket No. 94-97, Phase I (DA 95-374), Order Designating Issues for Investigation, (Com. Car. Bur., released February 28, 1995) (Designation Order).

[2] Oppositions to SWBT's Direct Case were filed by Teleport Communications Group Inc. (TCG); MFS Communications Company, Inc. (MFS); Association for Local Telecommunications Services (ALTS); MCI Telecommunications Corporation (MCI); Time Warner Communications Holdings Inc. (Time Warner); Kansas City Fibernet, LP (FiberNet); and Electric LightWave, Inc. (ELI).

[3] TCG at 1-2, Fibernet at 4-5, ALTS at 8-10, MCI at 5-10, Time Warner at 6-7, and MFS at 2-5.

cost data, it is clear that these competitors of SWBT wish to view the information merely for their own competitive uses.

Perhaps the most curious of the Oppositions is the new position of ALTS, which now states that "SWBT has no sound basis for seeking confidentiality." ALTS had previously filed comments on SWBT's tariff with a confidential section of its own. If there is "no sound basis" to protect vendor prices, then why did ALTS file a portion of its comments under a request for confidential treatment? Indeed, the bulk of ALTS' attack on SWBT's confidentiality is an attack upon the Bureau's initial ruling on SWBT's confidential request, which found that the vendor data was, in fact, to be protected. If ALTS wishes to properly contest this ruling, it should have filed an application for review. It did not do so, and should not be heard now to argue with the Bureau's findings.[4]

MFS' arguments are also questionable. MFS claims that SWBT "has diverted already scarce Commission resources" to SWBT's arguments and that SWBT is "gaming" the regulatory process.

MFS fails to acknowledge that MFS has encouraged much of the difficulty in this regulatory process by urging the Commission to adopt its <u>Virtual Collocation Order</u> without the notice and comment that were properly required. In such a notice and comment proceeding, the difficulties with the Commission's virtual

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[4] ALTS claims that SWBT blatantly misportrays the tariff review process as it has existed throughout the Commission's six decade history and that the Commission has always relied upon the comments of informed intervenors. What ALTS neglects to recognize is that six decades ago the same need to keep cost data confidential did not exist because the current competition for LECs' services did not exist.

collocation policy may have been solved at an early stage in the process. Instead, the Commission, and the industry, are now forced to deal with the difficulties of the policy on an ongoing basis -- a process which takes more effort.[5] While MFS complains about the absence of a final ruling on SWBT's Application for Review, MFS should not direct its complaints to SWBT's Direct Case, but to the Commission, which controls the speed at which it will issue that ruling.[6]

Time Warner complains that SWBT's Direct Case is "the most egregious example of noncompliance."[7] Time Warner, however, provides no reason that it should be allowed to see SWBT's confidential cost data, or why the Commission should violate precedent in order to allow Time Warner to see that data. While Time Warner complains that SWBT's request is far beyond that of any other LEC, Time Warner fails to recognize that SWBT has filed, with the Commission, the most extensive set of confidential equipment prices of any LEC.

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[5] MFS continues to argue that a reasoned analysis of SWBT rates can only occur with full knowledge of SWBT's costs. As SWBT has previously explained in its Application for Review of the Bureau's November 1, 1994 letter ruling, MFS need only be aware of SWBT's rates to analyze them against its own costs. MFS' unwillingness to offer up detailed evidence of its own cost structure in comparison to SWBT's rates supports SWBT's position on confidentiality.

[6] It should be noted that in the process of negotiating virtual collocation arrangements, MFS offered to sell equipment to SWBT, but insisted that SWBT keep the prices of MFS' equipment confidential. This request stands in stark contrast to the public position MFS takes here -- that SWBT should be required to make its own equipment cost public.

[7] Time Warner at p. 6.

MCI claims that "the Commission requires that the cost support material necessary to make [a determination on the rates offered by the LECs] be filed on the record."[8] MCI, however, provides no authority for this statement. MCI further claims that SWBT, Ameritech and Cincinnati Bell offer no justification for confidential treatment in their direct cases. On the contrary, SWBT filed a request for confidential treatment, fully explaining its grounds for withholding the Direct Case confidential sections from public inspection. In any event, however, the Designation Order did not ask SWBT to provide such justification.

MCI goes on to make further arguments against SWBT's request for confidential treatment. MCI fails to recognize, however, that these arguments contradict the November 1, 1994 letter ruling from the Common Carrier Bureau which determined that SWBT's pricing data in this case was worthy of confidential treatment. MCI did not file an Application for Review of that ruling and should not now be heard to argue that it was incorrect.

II. NONE OF THE OPPOSITIONS CAN JUSTIFY THE BUREAU'S NEW DEFINITION OF "COMPARABLE SERVICES."

A. The Use Of The Term, "Most Favored Customer" Should Be Rejected As A Method To Determine The Proper Overhead For SWBT's Virtual Collocation Rate Elements.

The Oppositions confirm that there is much confusion over the Bureau's use of the term, "most favored customer." Fibernet claims that SWBT's clarification of the term, "most favored

[8] MCI at p. 6.

customer," is incorrect.[9] However, Fibernet adds more confusion to the issue. Mandating that the LEC charge interconnectors an overhead percentage equal to the lowest overhead percentage on any comparable service ensures that interconnectors will have an unearned cost advantage on most services. In fact, inasmuch as the rate elements the Commission chose for use in establishing interconnection overheads had little or no demand, SWBT will be at a disadvantage in virtually all cases. Not surprisingly, Fibernet supports this policy, and even goes so far as to indicate that:

> An equally efficient interconnector paying rates that include average overheads could only offer a competitively priced service (while recovering its costs) to those end users who were purchasing a SWBT-provided service with rates that contain a higher than average contribution to overhead. Conversely, an equally-efficient competitor could never offer a competitively priced service (while recovering its costs) to an end user who was purchasing a SWBT-provided service with rates that contain a lower than average contribution.[10]

This statement demonstrates the outrageousness of Fibernet's position. Fibernet desires to be guaranteed by regulatory fiat that its cost structure will always be superior to its LEC competitors. If the contribution on the interconnection input is always less than the LECs' comparable service configurations, then Fibernet will always have a marketplace advantage.

Just as each LEC service has an individual cost, and overhead loading, the same is true for Fibernet. Therefore, if Fibernet is equally efficient, it has cost and overhead variances

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[9] Fibernet at p. 13.

[10] Fibernet at pp. 13-14.

that likely track the variances experienced by the LEC. However, while the LEC is prohibited from recovering the proper overhead in the collocation rates, Fibernet will be able to recover any overhead amount it chooses in its own rates. This lack of parity is also aggravated by the fact that the LECs are required to offer service under highly averaged rates, so individual service contributions are of little marketplace importance. More importantly, in the business world, businesses compete on the basis that they can be more efficient than their competitors. This efficiency is gained by reducing costs, not by looking to the regulatory process to "rig" input prices so that one firm always has a cost advantage. The Commission should not guarantee an undeserved cost advantage to interconnectors and should affirm the use of average overhead loadings on interconnection elements.

MCI claims that the cost to interconnectors for LEC facilities should be equal to those the LEC charges itself, and thus the Bureau's view that the lowest overhead loading assigned to other DS1 and DS3 services should be used is proper.[11] MCI states this principle without properly following it to its logical conclusion. If the cost for interconnection facilities should be equal to those used by the LEC in its own services, MCI must then agree that SWBT's use of an average overhead amount is proper. The average amount includes <u>all</u> of those rates that "the LEC charges itself." MCI provides no basis for using only the lowest of these amounts.

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[11] MCI at p. 12.

Looking at the lowest overhead factor alone to find the alleged "most favored customer," or the most "comparable service" does not consider all the dynamics of competition and pricing, and provides no basis on which to determine pricing policy. In some cases, rate elements have a lower overhead factor, but comparable rate elements with a higher overhead factor are priced at a lower dollar amount per unit of service. The best course of action would be for the Bureau to simply refrain from attempting to determine who is a "most favored customer."

Much debate can be had over whether competitors lower their overhead factors, or overhead dollar amounts, in order to respond to competition. In reality, however, competitors enter a geographic market and attempt to acquire as much business as possible, no matter what rate plan a customer may currently use. Any attempt to decide that a customer using a certain rate plan is more or less likely to face competition is therefore misguided.

B. "Rate Elements" Should Not Be Confused With "Services."

The Oppositions continue to confuse the term "rate element" with "service."[12] No party has refuted SWBT's contention that the Bureau's characterization of a rate element as a service is at odds with the record in CC Docket No. 83-1145. Fibernet's[13] characterization of this issue as a play on words does not address the Bureau's apparent departure from precedent in the determination of a comparable service.

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[12] Fibernet at pp. 14-15.

[13] Fibernet at p. 15.

SWBT's Direct Case cited CC Docket No. 83-1145 in response to a portion of question 17(e): "SWB, for example, must explain why it characterized its comparable DS1 and DS3 services that provide channel terminations without interoffice mileage as 'rate elements'."

SWBT explained the basis for rate structure associated with the initial special access tariffs resulting from divestiture. Simply stated, the presence of interoffice mileage is transparent to the service provided to the customer. Interoffice mileage is used based upon geography rather than the service requested by a customer. Therefore, it is inappropriate to exclude channel mileage from the determination of the overhead included in a comparable service. If DS1 and DS3 are considered the "comparable services" all components of DS1 and DS3 service should be included in the determination of the overhead.

Fibernet states LEC customers truly are purchasing rate elements, and services exist only as a collection of rate elements. This supports SWBT, which has stated that channel terminations are a rate element or component of the service provided to a customer. Fibernet, however, also states on page 15 that the use of a rate element to determine a comparable service is fully supported by Fibernet as a means to implement the most favored customer policy articulated by the Bureau. Therefore, it is not clear how Fibernet defines a service. Fibernet essentially claims that the bundling of rate elements into services is an artificial construct created by the LECs through the tariffing process.

This position, however, disregards Commission orders in CC Docket No. 78-72 (the private line rate structure guidelines) and the Part 61.40 rules. Ironically, if the bundling suggested by Fibernet were present in the existing rate structure, channel mileage would be included in the overhead associated with the Bureau's selected comparable service.

ALTS (on page 5) supports the use of a single rate element to determine the appropriate level of overhead and claims that the LECs, including SWBT have failed to justify the overheads reflected in the proposed collocation rate elements. On page 15 ALTS proceeds to state that SWBT is refusing to confront the underlying issue of the allocation of overhead to its own comparable services and functionalities and that this refusal is evidence of predatory intent.

Assuming, arguendo, that virtual collocation is comparable to DS1 or DS3 service, the comparable nature is in general terms based upon the type of cross connect requested. DS3 service provides the best example. SWBT provides DS3 through 32 basic options - electrical or optical in volume options of 1, 3, 6 or 12 for terms of 1, 3, 5 or 10 years. Whether or not channel mileage is present is not a customer option as channel mileage is a physical routing requirement based upon the geographic relationship between point A and point B.

If comparable service is to be defined as a specific service configuration or a single rate element, SWBT must agree with the other LECs that state that they do not offer a comparable service. This conclusion is necessary as the rate elements associated with virtual collocation are not comparable to any single rate element or single service configuration available in SWBT's access tariff.

The correct answer to the question of comparable service is straightforward -- DS1 and DS3 special access service. DS1/DS3 service is the hand-off to the customer of a DS1 or DS3 signal. DS1 and DS3 service utilizes the rate elements contained in the DS1 and DS3 service category of the Trunking Basket of price cap regulation. The contrary position, apparently espoused by the Bureau, is that individual rate elements are services. This position results in the elimination of certain rate elements required for end-to-end service in the determination of the overhead factor.[14]

Time Warner's position is unclear.[15] Time Warner (on page 13) appears to support the use of a single rate element to determine "comparable service," but then on page 16 Time Warner states discounted offerings should be included in the scope of comparable services. (Time Warner further states the overhead loading on month-to-month virtual collocation rate elements should be comparable to DS1 and DS3 discounted offerings.) The apparent

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[14] ELI on page 4, chastises U S WEST for narrowly defining only DS1 and DS3 channel terminations for single circuits taken on a month to month basis as comparable services. ELI states this is an unreasonable position. The Bureau's selection of a single rate element as a comparable service is virtually identical to the selection process deemed unreasonable by ELI.

McLeod TeleManagement, Inc. (McLeod), on page 3, quotes the Tariff Review Plan order that stated comparable services include channel mileage. McLeod apparently does not dispute that channel mileage is a component of "comparable service."

[15] Time Warner at p. 13.

solution to Time Warner's complaint is to use the SWBT approach -- all DS1 and DS3 offerings.

C. None Of The Interconnectors Can Refute SWBT's Presentation Of A Comparable Service.

SWBT's Direct Case presented concrete data comparing the price of a technically equivalent DS3 service configuration offered by SWBT with SWBT's virtual collocation offering as a demonstration of the extreme discounting mandated for interconnection rate elements. This comparison used one of the many comparable service configurations that make up the universe of services with which the CAPs wish to compete. The intervenors offered no meaningful response.[16]

In total, the intervenors apparently desire that the Bureau should simply ignore SWBT's direct comparison. However, as the Direct Case demonstrates, virtual collocation at the rates prescribed by the Bureau are merely hyper-discounted versions of SWBT's MegaLink Custom Optical services minus the additional fiber provided by the interconnector.

Interconnectors compete with a wide range of services, not just one comparable service configuration. The Bureau concluded that "[i]f a LEC were to use an average overhead loading

[16] MFS at p. 15, claims that SWBT overstated the cost of MegaLink Custom Optical service by including the costs of terminating equipment at the customer premises. MFS is incorrect. The service compared does not include electronics on the customer's premises. SWBT stated in the comparison that local loop plant was not removed from the analysis. As the reduction ordered by the Commission results in a 76% discount for the interconnector over the technically comparable service configuration, exclusion of loop plant costs is inconsequential. TCG also incorrectly attempts to convince the Commission that Megalink Custom Optical services include electronics on the customer premises. TCG at p. 1.

factor for services provided to interconnectors and a below-average loading factor for LEC services with which the interconnectors compete, the effect would be to hamper the ability of the interconnectors to compete effectively."[17] SWBT's Direct Case refuted this conclusion by demonstrating that SWBT does not assign below average overheads on services with which interconnectors compete. In contrast, the Commission's unlawful RAF forces SWBT to charge unreasonably discounted rates to interconnectors, resulting in SWBT being forced to compete using average overheads while interconnectors are all charged below average overheads. Obviously, this prevents SWBT from competing effectively.

SWBT demonstrated that the interconnectors compete with a wide range of LEC services, all of which make up the average overhead percentage assigned by SWBT to interconnection elements. MFS apparently confirms this point since it indicated that "the list of comparable services should include all LEC services against which interconnectors may compete."[18] This is the correct position as long as all of these services are used to develop a composite overhead loading. SWBT has used precisely this method -- charging interconnectors an average overhead that considers all the service configurations for which the interconnectors compete.

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[17] Virtual Collocation Tariff Order at para. 23.

[18] MFS, p.14.

D. "Promotional Offerings" Should Not Be Considered "Comparable Services."

Some of the Oppositions attempt to show that "promotional offerings" should be considered "comparable services."[19] None of these oppositions, however, justified the inclusion of promotional offerings.

The Oppositions' efforts to use promotional rates are nothing more than thinly camouflaged attempts to prevent SWBT from using promotional rates in its DS1/DS3 services. At times, all businesses wish to have the ability to sell their products at less than the usual price in order to acquaint new customers with the services. This is a legitimate choice for the business, even though it means that profits from the service may be reduced for a short time. At other times, a business may want to heavily advertise the new service. While this choice may also decrease the profit for a short time, it would not reduce the overhead. SWBT should not be penalized for choosing (where it is legally allowed to do so) to sell one of its services at a lower price for a brief period.

The Oppositions, by their arguments, should not have the effect of regulating the methods by which SWBT can sell their DS1/DS3 services. Such regulation is outside the scope of this proceeding.

[19] Fibernet at pp. 17-19, MFS at pp. 19-22 and ALTS at pp. 15-17.

E. The Oppositions' Fears Of A "Price Squeeze" Are Unfounded.

The issue of an anticompetitive price squeeze, although raised by some of the parties in this case,[20] should not be an issue of concern in this case. An anticompetitive price squeeze would involve a LEC raising the price of its upstream factor (i.e., wholesale service) while simultaneously lowering the price of its downstream final service to such a point as to preclude a more efficient downstream provider from offering service. One sufficient condition to avoid a price squeeze is that the total dollar amount of contribution obtained by the LEC from selling its retail service to end users is no less than the total dollar amount of contribution that the LEC would have obtained simply from the sale of its upstream wholesale services. Stated in reverse, the total dollar amount of contribution from the upstream or wholesale service which would have been obtained should be no greater than the dollar amount of contribution obtained from the retail downstream service.[21] This standard is well established in the economics literature on imputation.[22]

The potential for a price squeeze can only be evaluated in the context of both the upstream and downstream total dollar

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[20] Fibernet at p. 6; TCG at p. 2.

[21] Equal percentage contributions for wholesale and retail services is generally an over-strong test to preclude an anticompetitive price squeeze.

[22] See, e.g., William J. Baumol & J. Gregory Sidak, Toward Competition in Local Telephony 94, 95-97 (1994); William J. Baumol & J. Gregory Sidak, The Pricing of Inputs Sold to Competitors, 11 Yale J. on Reg. 171 (1994); Alexander C. Larson & Steve G. Parsons, Imputation Policies and Competition in Telecommunications, 16 Hastings Comm/ent L.J. 1, 3 n.4 (1993).

contribution levels. There is no way in which to examine the price or contribution level of the upstream wholesale service by itself and conclude that the price is too high and that there exists an anticompetitive price squeeze. An anticompetitive price squeeze which has any policy implications can not exist if the retail competitor has higher costs than the LEC.

Perhaps more importantly, the LECs have no incentive to engage in an anticompetitive price squeeze. An anticompetitive price squeeze by nature would cause the contribution and profits obtained by the LEC to be lower than they otherwise would be. In fact, the modern economics literature indicates that neither predatory pricing in general nor anticompetitive price squeezes in particular are at all common in American industry.[23] Generally, the key to evaluating any claims of an anticompetitive price squeeze, for instance, in a hypothetical numerical example, is to carefully determine if the downstream competitor has higher costs than the LECs. In virtually all cases, numerical "examples" of anticompetitive price squeezes are really examples of either a "squeeze" which earns less profit for the LEC, or of squeezing a less efficient rival out of the market.

One other important factor to bear in mind while evaluating claims of anticompetitive price squeezes is that downstream competition will occur first in those segments with the

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[23] Authors arguing that predatory pricing is so rare and irrational that antitrust law should ignore it include: Robert Bork, <u>The Antitrust Paradox</u> (1978); Frank H. Easterbrook, <u>Predatory Strategies and Counterstrategies</u>, 48 U. Chi. L. Rev. 263 (1981); John S. McGee, <u>Predatory Price Cutting</u>: The Standard Oil (N.J.) Case, 1 J.L. & Econ. 137 (1958); John S. McGee, Predatory Pricing Revisited, 23 J.L. & Econ. 289 (1980).

lowest costs and the highest contribution. The price of an upstream input such as interconnection, must only be no higher than a level which would provide the same contribution as the LECs sale of the full retail service. Competitors will necessarily be drawn to the high contribution areas, which suggests that contribution on retail services further lessen the potential for an anticompetitive price squeeze.

F. MFS' Misrepresentations Should Be Rejected.

MFS misrepresents SWBT's Direct Case by stating that SWBT employs different annual cost factors for DS1/DS3 service as compared to virtual collocation. What SWBT stated was that annual cost factors were used in exactly the same way for virtual collocation as with any other service. The only difference was the vintage of the factors and the use of a company factor vs. the weighted average of state costs produced with state specific factors (which produces equivalent results).

MFS also misrepresents SWBT's use of annual cost factors in Transmittal 2268 as overhead factors.[24] The overhead factors are different.

[24] The annual cost factors listed by MFS are factors that identify the direct costs associated with the service and are not overhead factors. Yet MFS refers to a .012 overhead loading factor for maintenance and a.172 loading factor for capital costs. This type of characterization apparently results from a failure to properly analyze the data already made available and provides no reason to make additional data available, as MFS requests.

III. SWBT PROPERLY INCLUDED OVERHEAD LOADINGS ON NONRECURRING CHARGES FOR IDE.

Fibernet relies on the arguments of one of its owners (Time Warner), to state its opposition to SWBT's overhead practices on nonrecurring charges (NRCs).[25] Time Warner argues that SWBT should not be allowed to apply overhead loadings to its interconnection rate elements unless it applies overhead to its NRCs for DS1/DS3 offerings.[26] MFS takes the opportunity in its comments on this subject to again argue that SWBT should be forced to accept the "$1 deal."[27]

Fibernet is simply arguing that its entry into competition with the LECs would be much easier if the LEC will assume the risk of cost recovery for IDE through recurring rates. The rate structure developed by SWBT for virtual collocation clearly reflects the unique nature of the costs caused by Virtual Collocation. The Commission's virtual collocation requirement that interconnectors be allowed to designate equipment (IDE) to be placed in SWBT offices for their exclusive use distinguishes virtual collocation and the nature of the non-reusable equipment costs caused by virtual collocation from SWBT service offerings. SWBT has reflected this cost causation in the rate structure by recovering the cost of IDE in the same way that it is caused. It

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[25] Fibernet at p. 19.

[26] Time Warner at p. 28.

[27] MFS at p. 24. MFS continues this plea even though the Commission has stated that it cannot legally force SWBT to do so. Obviously, just as MFS encouraged the Commission to adopt what turned out to be an unlawful physical collocation policy, MFS fails to accept that fact, and continues to suggest that the Commission should commit another unlawful act.

is a logical extension of this cost recovery that overhead costs also be recovered through this same rate structure. Absent any cogent justification for changing SWBT's rate structure, the only appropriate response is to let the structure stand.

Fibernet claims SWBT has not explained the proposed rate structure.[28] The Designation Order required a justification for inclusion of overhead in nonrecurring charges. Rather than address the justification submitted, Fibernet attempts to divert the issue to a justification for nonrecurring charges. The justification for the recovery of capital associated with interconnection was included in SWBT Description and Justification in both the initial physical collocation and virtual collocation filings.

Time Warner at page 28 argues that overhead loadings should be removed unless the LEC applied equivalent loadings to its comparable DS1/DS3 services. However, Time Warner does not reconcile, at least in respect to SWBT, the fact SWBT's proposed interconnection nonrecurring charges do not represent the same costs reflected in SWBT's comparable services.

MFS claims that SWBT can reuse IDE. MFS conveniently ignores the huge list of equipment SWBT was required to file. Many of the equipment items included as Interconnector Designated Equipment (IDE) are not employed by SWBT in its network. SWBT cannot reuse IDE that is not part of SWBT's own network.

Also, utilization of IDE will represent either services currently provided by SWBT or growth circuits estimated by SWBT. In either case, IDE utilization will likely displace the

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[28] Fibernet at p. 21.

utilization of working SWBT facilities or facilities that have been placed to meet anticipated growth. Since IDE is nothing more than a duplication of the existing SWBT network IDE likely represents "overbuild" that is not useful to SWBT.

Finally, a required reuse of abandoned IDE could result in SWBT's required use of "last year's model." With the rapid changes in technology it is possible the IDE placed today would not be what SWBT would use for itself if purchased next year. SWBT and its customers should not be required to utilize outdated equipment due to the investment decisions of a competitor.

IV. THE PRESCRIBED RATE CAN BE CONFISCATORY EVEN THOUGH IT RECOVERS DIRECT COSTS.

MCI claims that a rate cannot be confiscatory if it allows for recovery of direct costs.[29] While MCI claims that SWBT's argument is "void of logic," it is MCI that reaches the wrong conclusion.

To the extent that overhead expenses are not included in the direct costs of providing virtual collocation, establishing prices for collocation at levels which prevent overhead cost recovery is confiscatory. Clearly, any firm whose prices recover only the direct costs of supplying individual services will fail to recover its overhead and thereby incur financial losses. This situation obviously is not sustainable in the long run.

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[29] MCI at pp. 14-15.

MCI presumably intends for LECs to recover overhead costs from the prices charged for services which MCI does not purchase.[30] Since LECs must recover all overhead costs to remain viable business entities, MCI's apparent recommendation would suggest price increases for those LEC services which MCI designates as appropriate for overhead cost recovery. Market conditions, however, might prevent complete LEC overhead cost recovery if the selected price increases are too high relative to prevailing demand characteristics.

Since MCI's suggestion cannot realistically be applied to all LEC services (i.e., set all LEC prices to recover only the direct costs of supplying each specific service), it must be viewed as an attempt to influence the Bureau to minimize those LEC prices for services MCI intends to purchase. The Bureau should recognize that, just as MCI's prices include more than the direct costs of supplying toll services, LEC prices, in the aggregate, must account for overhead costs. LEC interconnection rates which contribute toward the recovery of overhead costs cannot, on this basis alone, be deemed inappropriate, anticompetitive, discriminatory, or somehow "unfair."

V. CONCLUSION

For the reasons stated above, and in SWBT's Direct Case, SWBT respectfully requests that the Bureau end the investigation in this docket, remove the RAF imposed on SWBT's rates, and re-

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[30] These services may also be services in which MCI plans to compete.

establish the rates originally filed by SWBT for virtual collocation.

Respectfully submitted,

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